



## Memorandum

Date *JAN 15 2002*  
*Thomas D. Roslewicz*  
From Thomas D. Roslewicz  
Deputy Inspector General  
for Audit Services  
Subject

To Audit of Administrative Costs Claimed Under Parts A & B of the Health Insurance for the Aged and Disabled Programs – AdminaStar Federal, Inc. Indianapolis, Indiana (A-05-01-00023)

Neil Donovan  
Director, Audit Liaison Staff  
Centers for Medicare & Medicaid Services

This memorandum is to alert you to the issuance on **January 17, 2002**, of our final report. A copy is attached.

We suggest that you share this report with the Centers for Medicare & Medicaid Services' (CMS) components involved with monitoring the Medicare contractor financial operations, particularly the Office of Financial Management and the Center for Beneficiary Services.

The audit covered costs claimed by AdminaStar Federal (AdminaStar) on final administrative cost proposals for Fiscal Years 1998 and 1999. Costs claimed totaled \$193,455,170: \$81,763,259 for Part A, \$71,399,257 for Part B, and \$40,292,654 for durable medical equipment regional carrier (DMERC) operations.

Of the total claimed, we recommended a financial adjustment of \$4,694,863: \$2,171,529 for Part A, \$1,602,931 for Part B, and \$920,403 for DMERC operations. Adjustments are recommended because AdminaStar:

- overstated pension costs by \$1,736,538 because the costs were based on accrual accounting entries instead of actual cash contributions.
- claimed \$1,395,298 for post-retirement health benefit costs based on accrual accounting entries instead of actual cash contributions.
- claimed executive salary increases of \$599,960 which exceeded the average increases for comparable positions, as measured by a Federal Bureau of Labor Statistics Index.
- overstated employee benefit costs by \$451,660 because AdminaStar employee contributions were included in the costs charged to Medicare.

- claimed \$182,081 of deferred compensation costs based on accrual accounting entries instead of actual cash contributions.
- overstated return on investment costs by \$82,302 because AdminaStar's computations included errors and higher rates of return on investments than reported by Anthem, the parent corporation.

We also found that information to support the prior approval of leases and the volume of claims used to compute complementary credits was not available. We recommended that AdminaStar provide the necessary documentation to CMS for review. Adjustments to the Final Administrative Cost Proposals (FACP) should be made if necessary.

In addition, AdminaStar claimed costs on the FACP associated with the Indiana Gross Income Tax (IGIT) that is assessed based on a percentage of revenue. The findings of this report will reduce the costs claimed on the FACP and the corresponding Medicare revenue. Upon finalization of the FACP, we recommended that AdminaStar adjust costs claimed for the IGIT during the audit resolution process.

AdminaStar officials concurred in \$2,597,547 of our recommended financial adjustments (Pension Costs - \$503,565, Post-Retirement Health Insurance - \$1,395,298, Employee Benefits - \$451,660, and Clerical Errors - \$247,024). They also concurred in our recommendations on leases and complementary credits.

AdminaStar disagreed with the remaining \$2,097,316 of our recommended financial adjustments (Pension Costs - \$1,232,973, Executive Salary Increases - \$599,960, Deferred Compensation - \$182,081 and Return on Investments - \$82,302). AdminaStar did not respond to our recommendation for the IGIT. The full text of AdminaStar's comments is attached to our report.

For further information, contact:

Paul P. Swanson  
Regional Inspector General  
for Audit Services  
Region V  
(312) 353-2618

Attachment

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**AUDIT OF ADMINISTRATIVE COSTS  
CLAIMED UNDER PARTS A & B OF THE  
HEALTH INSURANCE FOR THE AGED  
AND DISABLED PROGRAMS**

**ADMINASTAR FEDERAL, INC.  
INDIANAPOLIS, INDIANA**



**JANET REHNQUIST  
INSPECTOR GENERAL**

**JANUARY 2002  
A-05-01-00023**



DEPARTMENT OF HEALTH AND HUMAN SERVICES  
OFFICE OF AUDIT SERVICES  
233 NORTH MICHIGAN AVENUE  
CHICAGO, ILLINOIS 60601

REGION V  
OFFICE OF  
INSPECTOR GENERAL

Common Identification No: A-05-01-00023

Mr. Michael McCarron  
President and Chief Operating Officer  
AdminaStar Federal, Inc.  
8115 Knue Road  
Indianapolis, Indiana 46250

Dear Mr. McCarron:

Enclosed for your information and use are two copies of an Office of Inspector General (OIG) audit report entitled, "Audit of Administrative Costs Claimed Under Parts A & B of the Health Insurance for the Aged and Disabled Programs." The audit covered the period October 1, 1997 through September 30, 1999. A copy of this report will be forwarded to the HHS action official named below, for her review and any action deemed necessary.

Final determination as to actions taken on all matters reported will be made by the action official. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG audit reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise. (See 45 CFR Part 5.)

To facilitate identification, please refer to the above Common Identification Number in all correspondence relating to this report.

Sincerely,

A handwritten signature in cursive script that reads "Paul Swanson".

Paul Swanson  
Regional Inspector General  
for Audit Services

Enclosures

**Direct Reply to HHS Action Official:**  
Ms. Opal Nealy  
Associate Regional Administrator

## SUMMARY

AdminaStar Federal, Inc. (AdminaStar) receives, reviews, audits and pays Medicare Part A claims under agreements that AdminaStar's parent corporation, Anthem, has with the Blue Cross and Blue Shield Association and the Centers for Medicare and Medicaid Services (CMS). In addition, AdminaStar receives, reviews, audits and pays Medicare Part B and DMERC claims under agreements that it has with CMS. AdminaStar is entitled to reimbursement for its allowable administrative costs incurred. For the period October 1, 1997 through September 30, 1999, AdminaStar claimed administrative costs on its Final Administrative Costs Proposals (FACP), as follows:

| <u>Fiscal<br/>Year</u> | <u>Part A</u>       | <u>Part B</u>       | <u>DMERC</u>        | <u>Total</u>         |
|------------------------|---------------------|---------------------|---------------------|----------------------|
| 1998                   | \$32,777,713        | \$36,864,068        | \$18,872,915        | \$ 88,514,696        |
| 1999                   | 48,985,546          | 34,535,189          | 21,419,739          | 104,940,474          |
| Total                  | <u>\$81,763,259</u> | <u>\$71,399,257</u> | <u>\$40,292,654</u> | <u>\$193,455,170</u> |

Of the \$193,455,170 in administrative costs claimed, we are recommending a financial adjustment of \$4,694,863: \$2,171,529 (Part A), \$1,602,931 (Part B), and \$920,403 (DMERC). These amounts are detailed by fiscal year and program in the Exhibits and the Findings and Recommendations section of the report.

The amounts questioned are summarized, as follows:

- Pension costs of \$1,736,538 were charged to Medicare based solely on accrual accounting entries instead of actual cash contributions.
- Post-retirement health benefit costs of \$1,395,298 were based solely on accrual accounting entries instead of actual cash contributions.
- Salary increases charged to Medicare for some executives exceeded average increases for comparable positions by \$599,960, when compared with a Federal Bureau of Labor Statistics index.
- Employee benefit costs of \$451,660 included the AdminaStar employee contributions in the costs charged to Medicare.
- A clerical error caused a cash draw of \$247,024 to be claimed as an expense.
- Deferred compensation costs of \$182,081 were based on accrual accounting entries instead of actual cash contributions.
- Return on investment (ROI) was overstated by of \$82,302 because AdminaStar's computations included errors and higher rates of return than reported by Anthem, the parent corporation.

Information to support (1) the prior approval of leases and (2) the volume of claims used to compute complementary credits was not available for our review. We recommend that AdminaStar provide the necessary documentation to CMS for review and adjustments to the FACP should be made if necessary.

In addition, AdminaStar claimed costs on the FACP associated with the Indiana Gross Income Tax (IGIT) that is assessed based on a percentage of revenue. The findings of this report will reduce the costs claimed on the FACP and corresponding Medicare revenue. We recommend that AdminaStar adjust the costs claimed for IGIT during the audit resolution process.

### **AdminaStar Response**

In a response to our draft report, AdminaStar officials concurred in \$2,597,547 of our recommended financial adjustments (Pension Costs - \$503,565, Post Retirement Health Insurance - \$1,395,298, Employee Benefits - \$451,660, and Clerical Errors - \$247,024). They also concurred in our recommendations on leases and complementary credits.

AdminaStar disagreed with the remaining \$2,097,316 of our recommended financial adjustments (Pension Costs - \$1,232,973, Executive Salary Increases - \$599,960, Deferred Compensation - \$182,081 and Return on Investments - \$82,302).

AdminaStar's response did not address our recommendation concerning the Indiana Gross Income Tax. Responses are summarized at the end of each finding and are attached as an Appendix to this report.

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## **INTRODUCTION**

### **BACKGROUND**

Health Insurance for the Aged and Disabled (Medicare) was established by Title XVIII of the Social Security Act. Hospital Insurance (Part A) provides protection against the cost of hospital and related care. Supplemental Medical Insurance (Part B) is a voluntary program that covers physician services, hospital outpatient services and certain other health services, such as durable medical equipment (DME). The Centers for Medicare and Medicaid Services (CMS) administers the Medicare program. Under an agreement with CMS, the Blue Cross and Blue Shield Association (BCBSA) participates as a Medicare intermediary to assist in program administration.

During our audit period, AdminaStar Federal (AdminaStar) was a subsidiary of Anthem Midwest, which itself was a subsidiary of Anthem Inc., a major insurance company.

Under a subcontract with BCBSA, AdminaStar receives, reviews, audits, and pays Medicare Part A claims. Under a separate agreement with CMS, AdminaStar participates as a Medicare carrier and performs the same functions for Medicare Part B. Under another separate agreement with CMS, AdminaStar participates as a Durable Medical Equipment Regional Carrier (DMERC) to process and pay DME claims for a ten state area.

Subject to limitations specified in the agreements, AdminaStar is entitled to reimbursement for reasonable administrative costs incurred. From October 1, 1997 through September 30, 1999, AdminaStar claimed \$193,455,170 in administrative costs.

### **SCOPE**

Our audit was conducted in accordance with generally accepted government auditing standards. The audit objective was to determine whether Medicare Parts A, B, and DMERC administrative costs claimed by AdminaStar on its "Final Administrative Cost Proposals" (FACP) were reasonable, allocable, and allowable. We examined the administrative costs claimed by AdminaStar to determine whether the amounts were in accordance with (i) Federal Acquisition Regulations (FAR) part 31, (ii) the Carrier/Intermediary Manual, and (iii) the Medicare agreements. We also reviewed the reasonableness of salary increases given to certain AdminaStar Federal, AdminaStar, Inc., and Anthem executives that were charged to Medicare.

Our examination included audit procedures designed to achieve our objectives and a review of accounting records and supporting documentation. The audit covered the period October 1, 1997 through September 30, 1999. Audit fieldwork was performed at AdminaStar offices in Louisville, Kentucky from November 2000 through May 2001.

Our audit did not cover pension segmentation. A separate audit of the AdminaStar pension plan for compliance with segmentation requirements will be performed at a later date.



## FINDINGS AND RECOMMENDATIONS

### PENSION COSTS

AdminaStar overstated the FACPs by \$1,736,538 because pension costs charged to Medicare were not funded by cash contributions. The costs charged to Medicare were based on accrual entries only. The Federal Acquisition Regulations (FAR), section 31.205-6(j)(2)(i), state that pension costs must be funded before the organization's Federal income tax return is due. Pension costs assigned to the current year, but not funded by the due date, are not allowable in a subsequent year.

### RECOMMENDATIONS

We recommend that AdminaStar:

1. Make a financial adjustment of \$1,736,538, as follows:

|       | <u>Part A</u>    | <u>Part B</u>    | <u>DMERC</u>     | <u>Total</u>       |
|-------|------------------|------------------|------------------|--------------------|
| 1998  | \$410,388        | \$434,415        | \$242,439        | \$1,087,242        |
| 1999  | <u>281,829</u>   | <u>220,903</u>   | <u>146,564</u>   | <u>649,296</u>     |
| Total | <u>\$692,217</u> | <u>\$655,318</u> | <u>\$389,003</u> | <u>\$1,736,538</u> |

2. Establish procedures to ensure that unfunded pension costs are not charged to Medicare.

### AdminaStar's Response

AdminaStar concurred with \$503,565 of our recommended financial adjustment on pension costs stating that FACPs covering calendar years 1997 and 1999 will be updated to disallow the claims. AdminaStar disagreed with the remaining \$1,232,973 questioned stating that the pension was funded by cash contribution in CY 1998 .

### OIG's Comments

Although Anthem, the parent company, contributed \$30 million to its pension fund in CY 1998, no documentation was available to support that any portion of this amount was applicable to AdminaStar.

### POST-RETIREMENT HEALTH INSURANCE

AdminaStar overstated post-retirement health insurance costs on the FACPs by \$1,395,298 because it did not fund its post-retirement plan in accordance with the Statement of Financial Accounting Standards (SFAS) No. 106 and applicable Federal regulations. Amounts claimed were based on accrual accounting entries, not cash contributions to an insurer, provider, or trustee.

The SFAS No. 106 requires that the expected costs of retiree health benefits be accrued during the employee's service years, rather than waiting for the costs to be incurred during retirement years. Assets must be segregated and restricted to provide for future benefits.

Federal regulations 48 CFR 31.205-6(o)(2) state that the retiree post-health benefit costs must be paid either to (i) an insurer, provider, or other recipient as current year benefits or premiums or (ii) an insurer or trustee to establish and maintain a fund or reserve for the sole purpose of providing health benefits to retirees. Retiree health benefit costs must be calculated in accordance with generally accepted actuarial principles and practices, and be funded by the time set for filing the Federal income tax return. Retiree health benefit costs assigned to the current year, but not funded or otherwise liquidated by the tax return due date, are not allowable in a subsequent year.

## RECOMMENDATION

We recommend that AdminaStar make a financial adjustment of \$1,395,298, as follows:

|       | <u>Part A</u>    | <u>Part B</u>    | <u>DMERC</u>     | <u>Total</u>       |
|-------|------------------|------------------|------------------|--------------------|
| 1998  | \$350,476        | \$372,946        | \$207,881        | \$ 931,303         |
| 1999  | <u>201,238</u>   | <u>165,184</u>   | <u>97,573</u>    | <u>463,995</u>     |
| Total | <u>\$551,714</u> | <u>\$538,130</u> | <u>\$305,454</u> | <u>\$1,395,298</u> |

## AdminaStar's Response

AdminaStar concurred with our recommendation.

## EXECUTIVE SALARY INCREASES

AdminaStar overstated the FACPs by \$599,960 for executive salary increases that exceeded the average increases for comparable positions, as measured by the Department of Labor, Bureau of Labor Statistics, Economic Consumer Index (ECI).

The ECI represents dozens of indices that are calculated for various occupational and industry groups to measure the rate of change in employee compensation. It is a fixed weight index at the occupational level and eliminates the effects of employment shifts among occupations. The ECI is distinguished from other surveys in that it covers all establishments and occupations in both the private non-farm and public sectors. We used the index for executive compensation because we considered it to be the most equitable and relevant measure.

For the executives in managerial/administrative occupations, the ECI showed the following average salary increases applicable to fiscal years (FY) 1998 and 1999.

|         |      |         |      |
|---------|------|---------|------|
| FY 1998 | 5.5% | FY 1999 | 3.9% |
|---------|------|---------|------|

We analyzed the salary increases for 21 executives (Vice President and above) at Anthem, Inc., AdminaStar, Inc., and AdminaStar who allocated time to the Medicare

contracts. The executive's salary increases exceeded the ECI averages by \$599,960 (Medicare share).

## **RECOMMENDATIONS**

We recommend that AdminaStar make a financial adjustment of \$599,960, as follows:

|       | <u>Part A</u>    | <u>Part B</u>    | <u>DMERC</u>     | <u>Total</u>     |
|-------|------------------|------------------|------------------|------------------|
| 1998  | \$130,005        | \$116,568        | \$ 64,636        | \$311,209        |
| 1999  | <u>155,430</u>   | <u>83,262</u>    | <u>50,059</u>    | <u>288,751</u>   |
| Total | <u>\$285,435</u> | <u>\$199,830</u> | <u>\$114,695</u> | <u>\$599,960</u> |

### **AdminaStar's Response**

AdminaStar officials disagreed with this recommendation stating that we did not consider factors such as, whether compensation conformed to compensation practices of comparable companies in the same industry, of the same size, in the same geographic region, or of companies engaged in predominately non-government work.

### **OIG's Comments**

The Department of Labor's ECI index was utilized for the express purpose of judging the reasonableness of the salary increases. We used this index because it is a widely recognized, unbiased, measure of industry-wide compensation practices.

## **EMPLOYEE BENEFITS**

AdminaStar incorrectly computed the employee benefit costs for FYs 1998 and 1999 and overstated the FACP by \$451,660. The amount charged to Medicare included AdminaStar employee contributions. FAR section 31.201-2(d) states that a contractor is responsible for accounting for cost appropriately and for maintaining records...adequate to demonstrate that costs claimed have been incurred, are allocable to the contract, and comply with applicable cost principles....

## **RECOMMENDATION**

We recommend that AdminaStar make a financial adjustment of \$451,660, as follows:

|       | <u>Part A</u>    | <u>Part B</u>    | <u>DMERC</u>    | <u>Total</u>     |
|-------|------------------|------------------|-----------------|------------------|
| 1998  | \$126,867        | \$134,502        | \$74,574        | \$335,943        |
| 1999  | <u>49,717</u>    | <u>40,948</u>    | <u>25,052</u>   | <u>115,717</u>   |
| Total | <u>\$176,584</u> | <u>\$175,450</u> | <u>\$99,626</u> | <u>\$451,660</u> |

### **AdminaStar's Response**

AdminaStar concurred with our recommendation.

## **CLERICAL ERROR**

AdminaStar erroneously reported an advance of \$247,024 from CMS as an expense on the FY 1998 Part A FACP. FAR section 31.201-2(d) state a contractor is responsible for accounting for cost appropriately ... adequate to demonstrate that costs claimed have been incurred, are allocable to the contract, and comply with applicable cost principles.

## **RECOMMENDATION**

We recommend that AdminaStar make a financial adjustment of \$247,024 to the FY 1998 Part A FACP.

### **AdminaStar's Response**

AdminaStar concurred with our recommendation.

## **DEFERRED COMPENSATION**

AdminaStar overstated deferred compensation costs on the FACP by \$182,081 because the costs were not funded with cash contributions. AdminaStar's deferred compensation plan is a supplemental form of pension plan offered to its "highly compensated" employees. The plan supplements AdminaStar's regular 401(k) plan. AdminaStar accrued deferred compensation costs based on estimates, without corresponding cash set aside, and charged the costs to Medicare.

Federal regulations at 48 CFR 31.205-6(j)(2)(i) state pension costs must be funded before the filing date of the Federal income tax return. Pension costs assigned to the current year, but not funded by the deadline, are not allowable in a subsequent year.

## **RECOMMENDATION**

We recommend that AdminaStar make a financial adjustment of \$182,081, as follows:

|       | <u>Part A</u>    | <u>Part B</u>   | <u>DMERC</u>    | <u>Total</u>     |
|-------|------------------|-----------------|-----------------|------------------|
| 1998  | \$ 57,373        | \$44,318        | \$24,592        | \$126,283        |
| 1999  | 43,380           | (734)           | 13,152          | 55,798           |
| Total | <u>\$100,753</u> | <u>\$43,584</u> | <u>\$37,744</u> | <u>\$182,081</u> |

### **AdminaStar's Response**

AdminaStar officials disagreed with this recommendation. Their response disagreed that the deferred compensation equates to a supplement pension plan and maintained that the OIG applied the incorrect federal regulation.

## OIG's Comments

Since AdminaStar's deferred compensation plan allows eligible executives to increase their retirement compensation, we do consider it to be a supplement pension plan. Plan proceeds may be distributed only upon retirement, either in 10 equal annual installments or a lump sum distribution. In our view, the pension plan regulations apply to the costs charged to Medicare.

## RETURN ON INVESTMENT

AdminaStar overstated the FACP by \$82,302 because it computed the rates of return incorrectly and used a higher rate of return than the portfolio rate of the parent, Anthem.

The AdminaStar computations for the rate of return included errors in the formulas for the net book values of fixed assets. We analyzed Anthem's trial balances and determined that Anthem's actual portfolio rate of return, which was 5.42 percent for FY 1998 and 5.50 percent for FY 1999, to be reasonable. We used these rates to compute the acceptable return on investment costs charged to Medicare.

## RECOMMENDATION

We recommend that AdminaStar make a financial adjustment of \$82,302, as follows:

|       | <u>Part A</u>    | <u>Part B</u>     | <u>DMERC</u>      | <u>Total</u>    |
|-------|------------------|-------------------|-------------------|-----------------|
| 1998  | \$ 39,262        | \$ 1,182          | \$(18,735)        | \$21,709        |
| 1999  | 78,540           | (10,563)          | (7,384)           | 60,593          |
| Total | <u>\$117,802</u> | <u>\$ (9,381)</u> | <u>\$(26,119)</u> | <u>\$82,302</u> |

## AdminaStar's Response

AdminaStar officials did not agree with the OIG using Anthem's rate of return on an annual basis. They believe that the rate should be computed on a monthly basis because the cost of money is computed monthly on the net book value of assets. AdminaStar plans to recalculate the Anthem portfolio rate of return on a monthly basis.

## OIG's Comments

We computed the return on investment in accordance with Medicare regulations, which state that the actual rate of the investment portfolio for the contract period, or a lower rate, be used to compute the cost of investment.

## LEASES

AdminaStar did not obtain prior written approval from CMS for several building leases, which exceeded the threshold amount specified by Medicare guidelines. Because AdminaStar's annual budget for administrative costs exceeded \$10 million, the threshold amount for written approvals is \$500,000 for the first year of the leases. This

requirement is applicable regardless of the charges to Medicare under Section 1750.5 of the Intermediary Manual Part I, Chapter VII.

The building costs charged to Medicare were \$669,707 (Indiana), \$1,880,820 (Kentucky), and \$572,625 (Ohio) during the first year of the leases.

## **RECOMMENDATION**

We recommend that AdminaStar submit the leases exceeding the threshold to CMS for determination of whether related costs are allowable.

### **AdminaStar's Response**

AdminaStar concurred with our recommendation.

## **COMPLEMENTARY CREDITS**

AdminaStar calculates complementary credits based on the volume of claims processed multiplied by the CMS approved rate per claim. The Office of Financial Management determines the approved rate per claim each year for Medicare Parts A, B, and DMERC. AdminaStar could not support the volume of claims shown on the FACPs for FYs 1998 and 1999.

The FAR 31.201-2(d) states that a contractor is responsible for accounting for costs appropriately and for maintaining records, including supporting documentation... adequate to demonstrate that costs claimed have been incurred, are allocable to the contract, and comply with applicable cost principles....

AdminaStar claimed complementary credits of \$15,853,305 on the FACPs, as follows:

|       | <u>Part A</u>      | <u>Part B</u>       | <u>DMERC</u>       | <u>Total</u>        |
|-------|--------------------|---------------------|--------------------|---------------------|
| 1998  | \$ 672,160         | \$ 5,120,435        | \$1,586,327        | \$ 7,378,922        |
| 1999  | <u>1,313,299</u>   | <u>5,322,096</u>    | <u>1,838,988</u>   | <u>8,474,383</u>    |
| Total | <u>\$1,985,459</u> | <u>\$10,442,531</u> | <u>\$3,425,315</u> | <u>\$15,853,305</u> |

Because AdminaStar did not provide documentation to support the volume of claims, there is no assurance that the FACPs contained appropriate credits to Medicare.

## **RECOMMENDATION**

Prior to finalization of the FACP, we recommend that AdminaStar provide documentation to CMS supporting the volume of claims used in computing complementary credits. Adjustments should be made if necessary.

### **AdminaStar's Response**

AdminaStar concurred with our recommendation.

## **INDIANA GROSS INCOME TAX**

AdminaStar claimed Medicare reimbursement for Indiana Gross Income Tax (IGIT) it paid to the state of Indiana. The tax rate is 1.2 percent of the Medicare reimbursement AdminaStar claimed on its Final Administrative Cost Proposals. The findings in this report will likely reduce the total amount of Medicare payments AdminaStar receives from CMS when CMS makes its final cost determinations.

## **RECOMMENDATION**

Upon finalization of the FACP, we recommend that AdminaStar adjust the amount of the IGIT charged to Medicare during the period covered by this audit proportionately to the final cost determinations.

### **AdminaStar's Response**

AdminaStar did not respond to our recommendation.

## **OTHER MATTERS**

The CMS requested that comments be included in this report concerning the accuracy of AdminaStar's Interim Expenditure Reports (IERs). We reviewed the methodologies used to prepare the IERs, and our limited testing did not disclose any material inaccuracies or weaknesses other than those disclosed in the findings of our report.

Subsequent to our fieldwork, AdminaStar filed revised FACP with CMS. We did not include these FACP in our scope of audit since these FACP were not prepared in time for us to review.

**Exhibit A**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (PART A)  
AND THE OIG RECOMMENDATIONS  
FOR THE FISCAL YEARS 1998 THROUGH 1999

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$23,009,288                |
| Appeals and Reviews                | 1,836,611                   |
| Inquiries                          | 6,133,350                   |
| Provider Education and Training    | 2,851,019                   |
| Reimbursement                      | 5,636,210                   |
| Productivity Investments           | 4,547,303                   |
| Complementary Insurance Credits    | (1,985,459)                 |
| Medical Review                     | 7,521,668                   |
| Medicare Secondary Payer           | 7,225,282                   |
| Benefit Integrity                  | 2,046,894                   |
| Provider Education and Training    | 1,221,374                   |
| Audit                              | 21,719,719                  |
| Total Administrative Costs Claimed | <u>\$81,763,259</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 692,217                     |
| Post Retirement Benefits           | 551,714                     |
| Executive Salary Increases         | 285,435                     |
| Employee Benefits                  | 176,584                     |
| Clerical Error                     | 247,024                     |
| Deferred Compensation              | 100,753                     |
| Return on Investments              | 117,802                     |
| Total Adjustments                  | <u>\$2,171,529</u>          |
| Costs Recommended For Acceptance   | <u>\$79,591,730</u>         |



**Exhibit B**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (PART B)  
AND THE OIG RECOMMENDATIONS  
FOR THE FISCAL YEARS 1998 THROUGH 1999

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$45,389,958                |
| Appeals and Reviews                | 5,535,393                   |
| Inquiries                          | 9,542,142                   |
| Provider Education and Training    | 1,070,640                   |
| Participating Physician            | 72,871                      |
| Productivity Investments           | 7,014,108                   |
| PM Special Projects                | 823,225                     |
| Complementary Insurance Credits    | (10,442,531)                |
| Medical Review                     | 5,847,556                   |
| Medicare Secondary Payer           | 3,611,018                   |
| Benefit Integrity                  | 2,350,364                   |
| Provider Education and Training    | 584,513                     |
| Total Administrative Costs Claimed | <u>\$71,399,257</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 655,318                     |
| Post Retirement Benefits           | 538,130                     |
| Executive Salary Increases         | 199,830                     |
| Employee Benefits                  | 175,450                     |
| Deferred Compensation              | 43,584                      |
| Return on Investments              | (9,381)                     |
| Total Adjustments                  | <u>\$1,602,931</u>          |
| Costs Recommended For Acceptance   | <u><u>\$69,796,326</u></u>  |

**Exhibit C**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (DMERC)  
AND THE OIG RECOMMENDATIONS  
FOR THE FISCAL YEARS 1998 THROUGH 1999

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$21,875,828                |
| Appeals and Reviews                | 4,881,412                   |
| Inquiries                          | 6,392,134                   |
| Provider Education and Training    | 636,778                     |
| Participating Physician            | 1,705                       |
| Productivity Investments           | 1,955,274                   |
| PM Special Projects                | 5,027                       |
| Complementary Insurance Credits    | (3,425,315)                 |
| Medical Review                     | 3,628,237                   |
| Medicare Secondary Payer           | 862,320                     |
| Benefit Integrity                  | 2,500,444                   |
| Provider Education and Training    | 978,810                     |
| Total Administrative Costs Claimed | <u>\$40,292,654</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 389,003                     |
| Post Retirement Benefits           | 305,454                     |
| Executive Salary Increases         | 114,695                     |
| Employee Benefits                  | 99,626                      |
| Deferred Compensation              | 37,744                      |
| Return on Investments              | (26,119)                    |
| Total Adjustments                  | <u>\$920,403</u>            |
| Costs Recommended For Acceptance   | <u><u>\$39,372,251</u></u>  |

**Exhibit D**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (PART A)  
AND THE OIG RECOMMENDATIONS  
FOR THE 1998 FISCAL YEAR 10/1/97-9/30/98

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$10,346,777                |
| Appeals and Reviews                | 776,675                     |
| Inquiries                          | 1,593,135                   |
| Provider Education and Training    | 971,139                     |
| Reimbursement                      | 2,218,947                   |
| Productivity Investments           | 1,545,613                   |
| Complementary Insurance Credits    | (672,160)                   |
| Medical Review                     | 2,765,434                   |
| Medicare Secondary Payer           | 2,645,021                   |
| Benefit Integrity                  | 864,931                     |
| Provider Education and Training    | 536,453                     |
| Audit                              | 9,185,748                   |
| Total Administrative Costs Claimed | <u>\$32,777,713</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 410,388                     |
| Post Retirement Benefits           | 350,476                     |
| Executive Salary Increases         | 130,005                     |
| Employee Benefits                  | 126,867                     |
| Clerical Error                     | 247,024                     |
| Deferred Compensation              | 57,373                      |
| Return on Investments              | 39,262                      |
| Total Adjustments                  | <u>\$1,361,395</u>          |
| Costs Recommended For Acceptance   | <u>\$31,416,318</u>         |

**Exhibit E**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (PART B)  
AND THE OIG RECOMMENDATIONS  
FOR THE 1998 FISCAL YEAR 10/1/97-9/30/98

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$24,188,653                |
| Appeals and Reviews                | 2,868,350                   |
| Inquiries                          | 4,253,952                   |
| Provider Education and Training    | 375,312                     |
| Participating Physician            | 64,624                      |
| Productivity Investments           | 3,943,204                   |
| Complementary Insurance Credits    | (5,120,435)                 |
| Medical Review                     | 2,622,298                   |
| Medicare Secondary Payer           | 1,935,704                   |
| Benefit Integrity                  | 1,302,510                   |
| Provider Education and Training    | 429,896                     |
| Total Administrative Costs Claimed | <u>\$36,864,068</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 434,415                     |
| Post Retirement Benefits           | 372,946                     |
| Executive Salary Increases         | 116,568                     |
| Employee Benefits                  | 134,502                     |
| Deferred Compensation              | 44,318                      |
| Return on Investments              | 1,182                       |
| Total Adjustments                  | <u>\$1,103,931</u>          |
| Costs Recommended For Acceptance   | <u>\$35,760,137</u>         |

**Exhibit F**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (DMERC)  
AND THE OIG RECOMMENDATIONS  
FOR THE 1998 FISCAL YEAR 10/1/97-9/30/98

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$10,806,735                |
| Appeals and Reviews                | 2,289,834                   |
| Inquiries                          | 2,759,768                   |
| Provider Education and Training    | 137,467                     |
| Participating Physician            | 1,705                       |
| Productivity Investments           | 474,520                     |
| PM Special Projects                | 5,027                       |
| Complementary Insurance Credits    | (1,586,327)                 |
| Medical Review                     | 1,589,744                   |
| Medicare Secondary Payer           | 312,293                     |
| Benefit Integrity                  | 1,199,983                   |
| Provider Education and Training    | 882,166                     |
| Total Administrative Costs Claimed | <u>\$18,872,915</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 242,439                     |
| Post Retirement Benefits           | 207,881                     |
| Executive Salary Increases         | 64,636                      |
| Employee Benefits                  | 74,574                      |
| Deferred Compensation              | 24,592                      |
| Return on Investments              | (18,735)                    |
| Total Adjustments                  | <u>\$595,387</u>            |
| Costs Recommended For Acceptance   | <u><u>\$18,277,528</u></u>  |

**Exhibit G**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (PART A)  
AND THE OIG RECOMMENDATIONS  
FOR THE 1999 FISCAL YEAR 10/1/98-9/30/99

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$12,662,511                |
| Appeals and Reviews                | 1,059,936                   |
| Inquiries                          | 4,540,215                   |
| Provider Education and Training    | 1,879,880                   |
| Reimbursement                      | 3,417,263                   |
| Productivity Investments           | 3,001,690                   |
| Complementary Insurance Credits    | (1,313,299)                 |
| Medical Review                     | 4,756,234                   |
| Medicare Secondary Payer           | 4,580,261                   |
| Benefit Integrity                  | 1,181,963                   |
| Provider Education and Training    | 684,921                     |
| Audit                              | 12,533,971                  |
| Total Administrative Costs Claimed | <u>\$48,985,546</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 281,829                     |
| Post Retirement Benefits           | 201,238                     |
| Executive Salary Increases         | 155,430                     |
| Employee Benefits                  | 49,717                      |
| Deferred Compensation              | 43,380                      |
| Return on Investments              | 78,540                      |
| Total Adjustments                  | <u>\$810,134</u>            |
| Costs Recommended For Acceptance   | <u><u>\$48,175,412</u></u>  |

**Exhibit H**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (PART B)  
AND THE OIG RECOMMENDATIONS  
FOR THE 1999 FISCAL YEAR 10/1/98-9/30/99

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$21,201,305                |
| Appeals and Reviews                | 2,667,043                   |
| Inquiries                          | 5,288,190                   |
| Provider Education and Training    | 695,328                     |
| Participating Physician            | 8,247                       |
| Productivity Investments           | 3,070,904                   |
| PM Special Projects                | 823,225                     |
| Complementary Insurance Credits    | (5,322,096)                 |
| Medical Review                     | 3,225,258                   |
| Medicare Secondary Payer           | 1,675,314                   |
| Benefit Integrity                  | 1,047,854                   |
| Provider Education and Training    | 154,617                     |
| Total Administrative Costs Claimed | <u>\$34,535,189</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 220,903                     |
| Post Retirement Benefits           | 165,184                     |
| Executive Salary Increases         | 83,262                      |
| Employee Benefits                  | 40,948                      |
| Deferred Compensation              | (734)                       |
| Return on Investments              | (10,563)                    |
| Total Adjustments                  | <u>\$499,000</u>            |
| Costs Recommended For Acceptance   | <u><u>\$34,036,189</u></u>  |

**Exhibit I**

ADMINASTAR FEDERAL, INC.  
FINAL ADMINISTRATIVE COST PROPOSAL (DMERC)  
AND THE OIG RECOMMENDATIONS  
FOR THE 1999 FISCAL YEAR 10/1/98-9/30/99

| <u>Operation</u>                   | <u>Administrative Costs</u> |
|------------------------------------|-----------------------------|
| Bills Payment                      | \$11,069,093                |
| Appeals and Reviews                | 2,591,578                   |
| Inquiries                          | 3,632,366                   |
| Provider Education and Training    | 499,311                     |
| Productivity Investments           | 1,480,754                   |
| Complementary Insurance Credits    | (1,838,988)                 |
| Medical Review                     | 2,038,493                   |
| Medicare Secondary Payer           | 550,027                     |
| Benefit Integrity                  | 1,300,461                   |
| Provider Education and Training    | 96,644                      |
| Total Administrative Costs Claimed | <u>\$21,419,739</u>         |
| Recommended Adjustments:           |                             |
| Pension                            | 146,564                     |
| Post Retirement Benefits           | 97,573                      |
| Executive Salary Increases         | 50,059                      |
| Employee Benefits                  | 25,052                      |
| Deferred Compensation              | 13,152                      |
| Return on Investments              | (7,384)                     |
| Total Adjustments                  | <u>\$325,016</u>            |
| Costs Recommended For Acceptance   | <u><u>\$21,094,723</u></u>  |



October 25, 2001

Ms. Lynn Barker  
HHS/OIG/Office of Audit Services  
101 West Ohio Street - Suite 750  
Indianapolis IN 46204

Re: CIN A-05-01-00023

Dear Ms. Barker:

We have received and reviewed your draft report for the FY1998 and FY1999 Audit of Administrative Costs Claimed Under Parts A & B of the Health Insurance for the Aged and Disabled Program for AdminaStar Federal.

AdminaStar Federal filed updated FACP's for FY1998 and FY1999 during the time the audit fieldwork was being performed. We will note where the updates occurred as we address each finding and recommendation. For the period October 1, 1997, through September 30, 1999, AdminaStar Federal claimed administrative costs as follows:

| <u>Fiscal Year</u> | <u>Part A</u> | <u>Part B</u> | <u>DMERC</u> | <u>Total</u>  |
|--------------------|---------------|---------------|--------------|---------------|
| 1998               | \$32,651,303  | \$36,749,156  | \$18,808,420 | \$88,208,879  |
| 1999               | \$48,755,079  | \$34,407,482  | \$21,350,993 | \$104,513,554 |
| Total              | \$81,406,382  | \$71,156,638  | \$40,159,413 | \$192,722,433 |

We concur with the findings and recommendations for **Post-Retirement Health Benefits, Employee Benefits, Clerical Error, Leases** and **Complementary Credits**. AdminaStar Federal has updated the FACP's for FY1998 and FY1999 to reflect the recommended adjustments for Post-Retirement Health Benefits and the Clerical Error.

We disagree with the finding in the area of **Pension Costs** because pension was funded by cash contributions for calendar year 1998. Cost Accounting Standard 412, paragraph 21.07 (2) states that to be allowable in the current year, pension costs must be funded by the time set for filing the Federal income tax return or any extension thereof. Pension costs assigned to the current year, but not funded by the tax return time, shall not be allowable in any subsequent year. The FY1998 and FY1999 FACP's have been updated to disallow pension costs related to October – December, 1997, and January – September, 1999.

We disagree with the finding in the area of **Executive Salary Increases** since no analysis was presented to us regarding the reasonableness of such executive salary increases. FAR 31.205-6 states that "compensation paid or accrued for each employee must be reasonable for the work performed." FAR 31.205-6, along with FAR 31.201-3, prescribes basic reasonableness tests as well as other factors that should be evaluated in assessing the reasonableness of compensation. Factors such as whether the compensation generally conforms to compensation practices of comparable companies in the same industry, of the same size, in the same geographic region or of companies engaged in predominately non-government work need to be considered. To our knowledge, none of these tests or other factors were considered in the determination of the finding. Rather,

**AdminaStar Federal**

A HCFA Contracted Carrier & Intermediary

the finding of excess executive compensation was based solely on the comparison of the Bureau of Labor Statistics Employment

Cost Index to the salary increase of certain Anthem and AdminaStar executives. We believe the compensation paid, and increases therein, to be reasonable within the context of normal and prudent business practices, industry norms as well as geographic norms. We also believe the compensation paid and the related increases conform to the meaning, intent and requirements of FAR 31-205.6.

We disagree with the finding in the area of **Deferred Compensation**. FAR 31.205-6(K) states that "deferred awards are allowable when they are based on current or future services." The audit finding equates deferred compensation with a supplemental pension plan, which it is not, and therefore applies the incorrect federal regulation. The provisions of 48CFR 9904.415 govern the measurement, allocation and accounting of deferred compensation and do not require current year funding of deferred compensation. Specifically, 48CFR 9904.415-40 states that "the cost of deferred compensation shall be assigned to the cost accounting period in which the contractor incurs an obligation to compensate the employee." The federal regulation cited in the finding is incorrect since it pertains to pension accounting.

We disagree with the finding in the area of **Return on Investment** because the auditors calculated and applied the Anthem portfolio rate of return on an annual basis. Because the cost of money is computed each month on the net book value of the assets, the portfolio rate of return should be calculated each month for an equitable rate of return. AdminaStar Federal will recalculate the Anthem portfolio rate of return on a monthly basis and provide a copy to the auditors for support.

In summary, AdminaStar Federal's position regarding the nine audit findings is as follows:

| Finding                          | OIG Position | AdminaStar Position             | Difference                           | FACP Submitted by AdminaStar |
|----------------------------------|--------------|---------------------------------|--------------------------------------|------------------------------|
| Pension Costs                    | \$1,736,538  | \$503,565                       | \$1,232,973                          | Yes                          |
| Post-Retirement Health Insurance | \$1,395,298  | \$1,395,298                     | \$0                                  | Yes                          |
| Executive Salary Increases       | \$599,960    | \$0                             | \$599,960                            | No                           |
| Employee Benefits                | \$451,660    | \$451,660                       | \$0                                  | No                           |
| Clerical Error                   | \$247,024    | \$247,024                       | \$0                                  | Yes                          |
| Deferred Compensation            | \$182,081    | \$0                             | \$182,081                            | No                           |
| Return on Investments            | \$82,302     | \$0<br>Determination<br>Pending | \$82,302<br>Determination<br>Pending | No                           |
| Leases                           | N/A          | N/A                             | N/A                                  | N/A                          |
| Complementary Credits            | N/A          | N/A                             | N/A                                  | N/A                          |
| Total                            | \$4,694,863  | \$2,597,547                     | \$2,097,316                          | N/A                          |

Sincerely,

A handwritten signature in black ink that reads "Michael McCarron". The signature is fluid and cursive, with the first name "Michael" and last name "McCarron" clearly distinguishable.

Michael McCarron

cc: Katherine M. Ewing (AdminaStar Federal)  
Glenn Rhodes (AdminaStar Federal)